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Combatting tax avoidance, the OECD way? The impact of the BEPS Project on developing and emerging countries' approach to international tax avoidance

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10 Annex

10.1 Topic list used in interviews

- Your general professional activities and how they have changed during the last years (as result of BEPS project or not)
- The tax administration's strategy towards tax collection
- Tax planning schemes used by foreign and domestic MNEs
- Notable international tax cases
- Process for achieving tax certainty from the tax administration (through tax rulings or other procedures)
- Exchange of rulings
- Tax incentives in country (and how they could be impacted by the BEPS project)
- Tax incentives: effective in attracting investors? Used to shift profits? Attracting mobile activities?
- Tax treaty policy: considerations in selecting treaty partners, articles, interplay domestic law and treaty
- Treaty shopping by inward investors and policy / administrative responses
- Effectiveness of anti-abuse rules in tax treaties of country
- MLI choices and implementation
- Obstacles to treaty ratification (DTAs and MLI)
- Disclosure requirements of multinational companies before BEPS
- Use by tax administration of country-by-country reports
- Data protection in country and trust in tax administration
- Transfer pricing: Use of transfer pricing guidelines and issues thereof
- Penalties for non-compliance with tax reporting requirements in India
- Litigation practices of tax administration before and after BEPS
- Dispute settlement before and after BEPS
- Evolution of objectives of international tax policies
- Public debates in country around tax avoidance / evasion
- Tax policy making process: What are the sources of international tax policy changes? Who participates in debates? Influence of industry, international advisors, political stakeholders

10.2 Table of interview participants

ID	*Country*	*Category*	*Number of people present*	*Date*
CO01	Colombia	Public Sector	1	2019
CO02	Colombia	Academic	1	2019
CO03	Colombia	Academic	3	2019
CO04	Colombia	Academic	1	2019
CO05	Colombia	Academic	1	2019
CO06	Colombia	Academic	1	2019
CO07	Colombia	Academic	1	2019
CO08	Colombia	Academic	1	2019
CO09	Colombia	Academic	1	2019
CO10	Colombia	Interest groups	1	2019
CO11	Colombia	Interest groups	1	2019
CO12	Colombia	Interest groups	1	2019
CO13	Colombia	Interest groups	1	2019
CO14	Colombia	Advisory	1	2019
CO15	Colombia	Advisory	1	2019
CO16	Colombia	Advisory	1	2019
CO17	Colombia	Advisory	1	2019
CO18	Colombia	Advisory	1	2019
CO19	Colombia	Advisory	1	2019
CO20	Colombia	Advisory	1	2019
CO21	Colombia	Advisory	2	2019
CO22	Colombia	Advisory	1	2019
CO23	Colombia	Advisory	1	2019
CO24	Colombia	Advisory	1	2019
CO25	Colombia	Advisory	1	2019
CO26	Colombia	Advisory	1	2019
CO27	Colombia	Advisory	1	2019
CO28	Colombia	Advisory	1	2019
CO29	Colombia	Advisory	1	2019
CO30	Colombia	Advisory	3	2019
CO31	Colombia	Business	1	2019
CO32	Colombia	Business	1	2019
CO33	Colombia	Business	1	2019
CO34	Colombia	Business	1	2019
CO35	Colombia	Business	2	2019
CO36	Colombia	Business	2	2019

ID	*Country*	*Category*	*Number of people present*	*Date*
CO37	Colombia	Public Sector	2	2019
CO38	Colombia	Public Sector	1	2019
CO39	Colombia	Public Sector	1	2020
IN01	India	Other	1	2019
IN02	India	Academic	1	2019
IN03	India	Academic	1	2019
IN04	India	Academic	2	2019
IN05	India	Academic	1	2019
IN06	India	Academic	1	2019
IN07	India	Academic	1	2019
IN08	India	Interest groups	1	2019
IN09	India	Interest groups	1	2019
IN10	India	Advisory	1	2019
IN11	India	Advisory	1	2019
IN12	India	Advisory	1	2019
IN13	India	Advisory	2	2019
IN14	India	Advisory	1	2019
IN15	India	Advisory	2	2019
IN16	India	Advisory	1	2019
IN17	India	Advisory	2	2019
IN18	India	Advisory	3	2019
IN19	India	Advisory	2	2019
IN20	India	Advisory	2	2019
IN21	India	Advisory	1	2019
IN22	India	Advisory	2	2019
IN23	India	Business	1	2019
IN24	India	Business	1	2019
IN25	India	Business	1	2019
IN26	India	Public Sector	1	2019
IN27	India	Public Sector	1	2019
NG01	Nigeria	Business	1	2022
NG02	Nigeria	Advisory	1	2022
NG03	Nigeria	Business	1	2022
NG04	Nigeria	Academic	1	2022
NG05	Nigeria	Advisory	1	2022
NG06	Nigeria	Academic	1	2022
NG07	Nigeria	Advisory	1	2022
NG08	Nigeria	Advisory	1	2022

ID	*Country*	*Category*	*Number of people present*	*Date*
NG09	Nigeria	Public Sector	1	2022
NG10	Nigeria	Public Sector	1	2022
NG11	Nigeria	Advisory	1	2022
NG12	Nigeria	Advisory	1	2022
NG13	Nigeria	Public Sector	1	2022
NG14	Nigeria	Advisory	1	2022
NG15	Nigeria	Public Sector	1	2022
NG16	Nigeria	Academic	1	2022
NG17	Nigeria	Public Sector	1	2022
SN01	Senegal	Public Sector	1	2022
SN02	Senegal	Advisory	1	2022
SN03	Senegal	Interest groups	1	2022
SN04	Senegal	Business	1	2022
SN05	Senegal	Advisory	3	2022
SN06	Senegal	Advisory	3	2022
SN07	Senegal	Advisory	3	2022
SN08	Senegal	Interest groups	1	2022
SN09	Senegal	Public Sector	1	2022
SN10	Senegal	Business	1	2022
SN11	Senegal	Business	1	2022
SN12	Senegal	Advisory	1	2022
SN13	Senegal	Public Sector	1	2022
SN14	Senegal	Public Sector	1	2022
SN15	Senegal	Public Sector	1	2022
SN16	Senegal	Public Sector	1	2022
SN17	Senegal	Advisory	1	2022
SN18	Senegal	Business	1	2022

10.3 Method to calculate treaty shopping risk

To summarize countries' policy approach with respect to treaty shopping, I calculate a treaty shopping risk indicator for each country-year-payment type, which I define as the difference between the weighted mean withholding rate and the minimum rate concluded with a potential conduit jurisdiction in the network. This indicator should show how the incentive to engage in treaty shopping has evolved in a country over time. Due to data limitations, I am only able to calculate this indicator for a sample of 59 developing countries for the time span 2004 to 2021. This limitation does not permit any comparison between developing and developed countries.

10.3.1 Data sources

Data on tax treaties concluded by developing countries is available from a dataset collected and published by Hearson and colleagues at the ICTD.[1] I extend this dataset by adding dates of treaty terminations sourced from IBFD's Tax Research Platform and other internet sources, in order to be able to reconstruct how each country's treaty network looked like in a given year. Finally, I use data on domestic withholding regimes and tax treatment of capital gains derived by non-residents from sales of shares for the years 2004 to 2021 from Ernst & Young's Global Corporate Tax Guides. I collected this data using a semi-automatic pdf extraction method.

As opposed to previous literature on treaty shopping,[2] I do not only consider the treatment of the three passive income flows (dividends, royalties, interest), but also the treatment of technical service payments, and taxation of capital gains at source. Evidence on specific countries shows that in particular the treatment of capital gains taxes can be more problematic in terms of base erosion. For example, many investors used Mauritius as conduit country to invest in India mainly due to the opportunity to avoid capital gains taxes.[3] Thanks to the ICTD Tax Treaties Database, comprehensive data in a machine-readable format is available for the treatment of these types of payments in tax treaties concluded by developing countries.

10.3.2 Calculation of treaty shopping risk

For each host country-year and each type of payment, I first calculate the mean withholding rate, weighted by the potential importance of a home country in inward investment flows. This indicator shows what withholding rate foreign investors would have to pay on average if they do not engage in treaty shopping. A weighted mean is used instead of the arithmetic mean, since not all home countries (and hence not all tax treaties) are equally relevant for each host country in terms of potential investment flows. "Potential importance" is a composite indicator consisting in the home country's GDP expressed as the share of all possible home coun-

1 The dataset is available at www.treaties.tax/ The version of the dataset used here is Version: 2.0.3. of 5 March 2021. According to the website, this version includes "treaties signed prior to 1 January 2020, status correct as of 29 August 2020, MLI positions correct as of 23 February 2021".

2 Petkova, Stasio, and Zagler, "On the Relevance of Double Tax Treaties"; Janský and Šedivý, "Estimating the Revenue Costs of Tax Treaties in Developing Countries"; Lejour, Möhlmann, and van 't Riet, "The Immeasurable Tax Gains by Dutch Shell Companies"; Van't Riet and Lejour, "Optimal Tax Routing: Network Analysis of FDI Diversion"; Arel-Bundock, "The Unintended Consequences of Bilateralism: Treaty Shopping and International Tax Policy."

3 Kotha, "The Mauritius Route: The Indian Response"; Robertson, "India's Offshore Pivot: The Implications of a Tougher Approach towards Mauritius."

tries' GDPs, the home country's GDP per capita and the physical distance between both countries.[4] This follows the intuition that any host country is more likely to receive FDI from a country, if it is 1) big, 2) wealthy, and 3) a neighbour. Hence, if for example, a country changes its bilateral outbound withholding rate with the USA, this is considered a more relevant change for relevant variables (such as tax revenue and investment) than if it changes its withholding rate with a country with a smaller economy such as for example Belgium. An alternative would be to use actual bilateral FDI flows or global FDI outflows from home countries as weights, but both indicators suffer from the distortions induced by treaty shopping. Actual bilateral FDI is difficult to observe due to the important role of conduit jurisdictions (and can only be estimated, based for example on data on conduit companies).[5] Therefore, I prefer the approach explained previously.

The second indicator I calculate for each country-year-payment type is the difference between the weighted mean withholding rate and the minimum rate concluded with a potential conduit jurisdiction in the network. A large difference between mean and minimum conduit rate indicates a high risk for treaty shopping, a small difference indicates a low risk. It may for example be observed that a treaty shopping risk indicator increases or declines, meaning that treaty shopping risk is increased or reduced. However, there are different ways how, for example, a decline in risk could come about: 1) The weighted mean rate declines, (e.g., if new treaties are signed or domestic rates are reduced) 2) the minimum conduit rate increases (e.g., if a treaty with a conduit jurisdiction is re-negotiated or terminated) 3) or a combination of both. These different causes for a change in treaty shopping risk may account of different overall strategies towards tax avoidance. If a country pursues 1), it essentially "gives up" to the pressures of treaty shopping and possibly tax competition with other countries. 2) is a strategy that seeks more to protect domestic resources. Of course, since treaties are bilateral (or in some cases multilateral) policies, a change in treaty shopping risk may not always be brought about by the country analyzed itself, but could also result from a policy change of the partner country, for example if the latter changed the law in a way that would make it more or less likely to be used as a conduit jurisdiction.

An alternative option would be to calculate indirect routes as other researchers have done.[6] However, the ICTD treaty dataset does not yet include treaties concluded among developed countries. For calculating indirect routes, however, a complete dataset of all tax treaties would be necessary. This should be done in future research.

4 GDP data comes from the World Bank and geographical distance from CEPII.

5 Damgaard, Elkjaer, and Johannesen, *What Is Real and What Is Not in the Global FDI Network?*

6 Arel-Bundock, "The Unintended Consequences of Bilateralism: Treaty Shopping and International Tax Policy"; Van't Riet and Lejour, "Optimal Tax Routing: Network Analysis of FDI Diversion."

10.3.3 Defining conduit jurisdictions

A challenging question is how to define which countries can be used as conduits in a given year. A conduit company has been defined by the OECD as "company situated in a treaty country [that] is acting as a conduit for channelling income economically accruing to a person in another State who is thereby able to take advantage 'improperly' of the benefits provided by a tax treaty."[7] Not all countries' legislations are suitable to set up conduit companies and channel income. Those that are could be identified using an empirical approach or using legal analysis.

Garcia-Bernardo et al. adopt an empirical approach, analysing which countries act frequently as intermediate jurisdiction in MNE's ownership chains and therefore potentially as conduit jurisdictions.[8] Through this method they identified the Netherlands, the United Kingdom, Switzerland, Singapore, and Ireland. The shortcoming of the empirical approach is that it may not be successful in uncovering smaller conduit jurisdictions, which at the global scale are not important but which could be relevant for individual jurisdictions. For example, while Spain might not be used as frequently as the jurisdictions mentioned above, its role as conduit jurisdiction for some Latin American countries is highlighted by practitioners and legal literature.[9] The empirical approach does not allow either to identify jurisdictions that may be suitable, but that have in practice not been used, for example because of a lack of promotion of the tax regime among practitioners. Finally, firm-level data is known for having incomplete jurisdictional coverage,[10] and firms might not react quickly to policy changes that might facilitate or hinder the use of a country as conduit jurisdiction. Therefore, I rely primarily on an analysis of the legal system to identify conduit jurisdictions.

The main characteristic of a conduit country is that it allows the MNE to pass through the flows with less costs than through a direct route, whereas typically no or little taxes are levied by the conduit country itself. Which countries can be used as conduit is analysed by types of income flow.

7 OECD, "Double Taxation Conventions and the Use of Conduit Companies," 2.
8 Garcia-Bernardo et al., "Uncovering Offshore Financial Centers."
9 CO01, CO07, CO28. See also Jiménez, "Las Entidades de Tenencia de Valores Extranjeros Como Instrumento de Planificación Fiscal."
10 Tørsløv, Wier, and Zucman, "The Missing Profits of Nations," 5–7.

Table 10: Characteristics of conduit jurisdictions

Type of flow from country or of origin	Characteristics of conduit jurisdiction
Dividend (above participation threshold)	• 0% corporate tax rate or • Participation exemption/territorial regime and 0% withholding tax for dividend or interest
Capital gains (shares / land-rich)	• 0% corporate tax rate or • Participation exemption/territorial regime and 0% withholding tax for dividend or interest or capital gains derived by non-residents
Interest	• 0% corporate tax rate or • 0% interest withholding or • 0% tax on interest income received from abroad and 0% withholding tax for dividend or interest
Royalties	• 0% corporate tax rate or • 0% royalties or interest withholding or • 0% tax on royalties received from abroad and 0% withholding tax for dividend
Technical services	• 0% corporate tax rate or • 0% services withholding

Source: the author

For each category, I assessed if the country has a special tax regime with the features mentioned above, if the features are not available in the normal tax regime (e.g., holding or headquarter regimes, IP or financing regimes, or services centre regimes).

For payments which are usually deductible as costs (such as interest, royalties, and technical services), it is generally not a requirement that a 0% corporate tax rate be levied on such foreign income, since income can be matched with costs incurred from another jurisdiction.[11]

One can also assume that companies can switch the nature of the flow when passing it through a conduit.[12] Lejour et al. empirically investigated to what extent companies switch the character of flows by comparing yearly cross-border in- and outflows of Dutch SPEs, using firm-level data on dividend, interest and royalty flows.[13] They estimate that companies do indeed switch between dividend, interest, and royalty. However, they find that in practice the figures for changes between royalty and interest

11 Lejour, Möhlmann, and van 't Riet, "The Immeasurable Tax Gains by Dutch Shell Companies."

12 Avi-Yonah and Panayi, "Rethinking Treaty-Shopping: Lessons for the European Union," 24; United Nations, "Contributions to International Co-Operation in Tax Matters. Treaty Shopping, Thin Capitalization, Co-Operation between Tax Authorities, Resolving International Tax Disputes," 5.

13 Lejour, Möhlmann, and van 't Riet, "The Immeasurable Tax Gains by Dutch Shell Companies."

flows are low.[14] Indeed, this type of change may not matter a lot since the tax treatment of interest and royalty is often the same. In addition, it seems conceptually more difficult to transform a financial flow into a royalty for services flow. Therefore, in addition to investigating treaty shopping strategies where the same type of payments flows through the conduit country, I assume that all kinds of flow can be transformed into a financial flow (i.e., dividend or interest).

This approach is restrictive in the sense that it only considers situations where companies can pass the income completely free of tax through the conduit, hence excluding those countries where a small amount of tax would be levied, which might still result in an advantage for the MNE.

On the other hand, the approach may be too wide, since not all countries with a tax regime suitable for setting up conduit companies might be effectively usable as such, for example because there is too much uncertainty around the applicability of the tax regime or because there are other business risks, such as expropriation or exchange controls. To address this issue at least partially, I excluded countries with heavy exchange restrictions, which I define as having a normalized Chinn-Ito index of 0.4 or less.[15] However, I do not apply this exclusion to countries with special regimes such as holding or headquarter regimes, since it is likely that the regular exchange restrictions would not apply to these special regimes.

Another potential limit to the suitability of a country for conduit activities could be anti-avoidance rules. Even if a country levies 0% withholding tax on interest payments abroad, the country might not be suitable as a conduit if it imposes a rule restricting the deductibility of interest to related parties. However, earnings-stripping rules such as proposed in BEPS Action 4 should not hinder conduit companies, since they typically apply only to the difference between interest deducted and interest received,[16] that is they do not apply where the payments made are matched by payments received, which would be the case in the conduit scenario. CFC rules should have no impact since the companies involved in the typical treaty shopping scheme are either engaged in an active business or do not make profits. Finally, BEPS Action 5 mandates countries to introduce substance requirements for their low-tax regimes. However, with respect to holding company regimes, the Action 5 report is relatively imprecise concerning the necessary substance requirement, and with respect to regimes that only provide for low taxation of income from dividends and capital gains, it assumes that

14 Lejour, Möhlmann, and van 't Riet, 14.

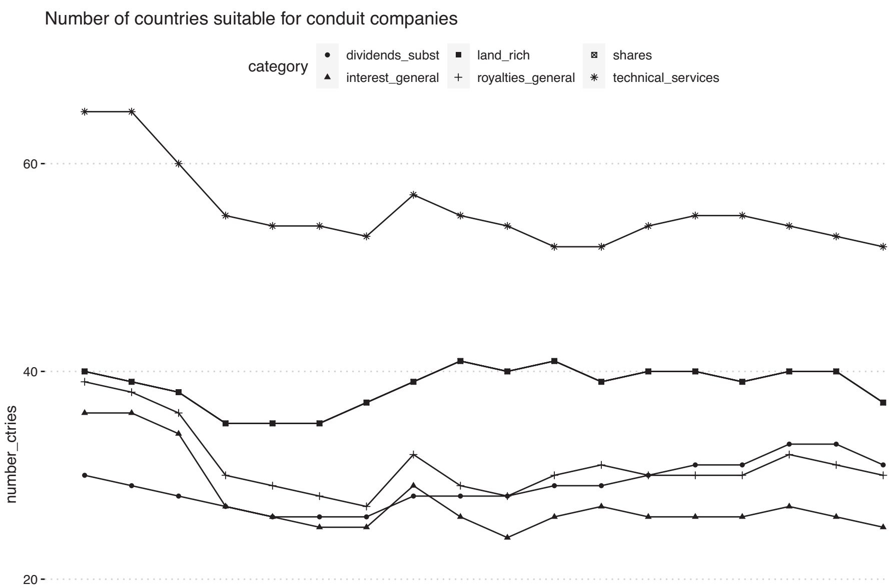
15 Chinn and Ito, "What Matters for Financial Development? Capital Controls, Institutions, and Interactions."

16 OECD, *Limiting Base Erosion Involving Interest Deductions and Other Financial Payments, Action 4 - 2016 Update*, 41–42.

the work under other Action items may be sufficient.[17] In general, however, substance requirements requiring heavy investment in tangible capital and employment requirement, such as often found in free trade zone regimes would likely make the use of the regime as a conduit too costly. For IP regimes with nexus requirements in place, it can be assumed that these are less likely to be useful in treaty shopping structures. Therefore, I take nexus requirements into account in the analysis of whether a country can be used as a conduit country and I do not include special low tax regimes, where the description conveys that the regime is only available for companies with significant substance.

Figure 18 shows the evolution of the number of countries that have tax regimes that are suitable for serving as conduit for the different types of payments. On average the number has not significantly changed since 2004. For dividends, it has slightly increased, presumably due to the fact that more countries have introduced participation exemption regimes.[18] For royalties, technical service payments, and interest, the number has somewhat decreased.

Figure 18: Number of countries suitable for conduit companies



Source: compiled by the author, based on ICTD Tax Treaty Dataset and EY Corporate Tax Guides.[19]

17 OECD, *Preventing the Granting of Treaty Benefits in Inappropriate Circumstances, Action 6 - 2015 Final Report*, 39–40.

18 Shin, "Why Do Countries Change the Taxation of Foreign-Source Income of Multinational Firms?"

19 Hearson, "Tax Treaties Explorer [Online Database]"; EY, "Worldwide Corporate Tax Guides."

10.3.4 Using conduits for service payments

Do companies treaty shop for reduced withholding tax on payments for technical services? Most studies on treaty shopping only study passive income flows.[20] However, for developing countries which levy withholding taxes on payments for technical services (or sometimes other services), and where a treaty provides for a reduction or elimination of such withholding tax, the question might arise.

One could assume that providing services always requires some substance (e.g., employees who perform the services) and that therefore companies cannot route service payments through conduit companies. Nevertheless, even if a company in a country B may enter into a contract for the provision of such services to residents of a country B, the company could probably subcontract a company in a third country C for the totality of the contract, thus effectively routing an income flow from country A to country C through country B, possibly taking advantage of a treaty between country A and country B. This may be even easier for services that can be automated to some extent, for example financial services or payments for software which are not classified as royalties. For example, so-called “software as a service” is classified as technical service in Brazil.[21] Harris asserts that “services are commonly provided by foreigners into a source State through tax havens.”[22]

The empirical evidence on the phenomenon is scarce, however. Johannesen et al. found, using data from German companies that service payments to affiliates are made disproportionately to companies in low tax jurisdictions. However, they do not assess whether the services are effectively rendered from these jurisdictions (i.e., whether companies engaged in treaty shopping or not).[23]

Through BEPS Action 6, an example was added to the Commentary to the OECD Model Convention (“Example G”), which deals with the provision of management, legal, and financing services to group subsidiaries established in different countries from a location that has been chosen, among others, for its tax advantages. The example suggests that such a situation should not lead to a denial of benefits, if the services “constitute a real business through which [the company] exercises substantive economic functions, using real assets and assuming real risks, and that business is carried on by [the company] through its own personnel located in [the country]”.[24]

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20 Lejour, Möhlmann, and van ’t Riet, “The Immeasurable Tax Gains by Dutch Shell Companies”; Petkova, Stasio, and Zagler, “On the Relevance of Double Tax Treaties”; Janský and Šedivý, “Estimating the Revenue Costs of Tax Treaties in Developing Countries.”

21 Kjærsgaard, “Allocation of the Taxing Right to Payments for Cloud Computing-as-a-Service,” 400.

22 Harris, “Chapter V: Neutralizing Effects of Hybrid Mismatch Arrangements,” 294.

23 Hebous and Johannesen, “At Your Service! The Role of Tax Havens in International Trade with Services.”

24 OECD, *Preventing the Granting of Treaty Benefits in Inappropriate Circumstances, Action 6 - 2015 Final Report*, 62.